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A Radical Change to Queensland's Rating and Land Tax System

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INGRAINED INTELLIGENCE

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A Radical Change to Queensland's Rating and Land Tax System

On 11 February 2010, the Queensland State government introduced the *Valuation of Land and Other Legislation Amendment Bill* 2010 into parliament. This Bill comes after lengthy and ultimately unsuccessful litigation with several major shopping centre owners.

In introducing the Bill, the Minster said that the intention was to respond to the recent Court of Appeal's decision in *Chief Executive, Department of Natural Resources and Mines v Kent Street Pty Ltd [2009]*. In that decision, the Court of Appeal dismissed the State's appeal against the Land Appeal Court's decision to reject the State's assertion that the unimproved value of improved land, for the purposes of levying land tax and rates, included the added value of any leases, the goodwill associated with the business conducted on the land, and an amount for any development premium or profit and risk associated with its previous development. As a consequence, the unimproved value for Pacific Fair Shopping Centre was assessed at $47.5 million, whereas the State had contended for a number of different values in the Land Court, the highest being $255 million.

The Minister, in a press release on 11 February 2010, said that it was the State's intention to "**correct** the Appeal Court's interpretation of the law". In doing so, the State obviously proposes to achieve what the Land Appeal Court has previously said amounted to a "radical change to the State's rating and land tax system"[1], affecting a variety of commercial properties "ranging from shopping centres of various sizes to central business district properties and various tourist attractions".[2]

The State appears to accept that in more recent years, it has adopted valuation practices that the Courts have determined were flawed. Rather than facing the consequences, however, the State proposes that the amendments will be retrospective, applying to all valuations in effect from 30 June 2002. The Explanatory Notes to the new Bill acknowledge that in doing so, the Bill infringes some "fundamental legislative principles," but states that the retrospective amendments are necessary to avoid, among other things, the State having to repay significant amounts of land taxes already charged.

The Minister has said that application of the Court of Appeal's decision would have resulted in a 20 percent reduction in valuations for industrial land, and a 35 percent reduction in valuations for commercial land[3].

With new unimproved valuations due for release in late March 2010 (valuations as at 1 October 2009 and with effect from 30 June 2010), it appears that the State intends to rush the new Bill through Parliament, protecting their land tax income stream and denying owners their much anticipated reductions in land valuation.

While the proposed amendments are aimed at protecting the State budget's bottom line in the short term, their legacy, in terms of the inevitable disincentive to investment in Queensland, will be with us for years to come.

Background

Benefits conferred by a development approval and other intangible assets such as goodwill, leases, agreements for lease and licences form a significant part of the value of a going concern.

In assessing the unimproved value of land for the purpose of levying land tax and rates, however, the *Valuation of Land Act* 1944 has long required that a valuer treat any improvements as if they "did not exist"[4]. In recent years, however, the State, in assessing the unimproved value of highly improved commercial properties, had effectively stated an amount for intangible improvements such as goodwill and the existence of leases including in those valuations.

In October 2007, after protracted litigation between the Department and several major shopping centre owners, the Land Appeal Court handed down its decision in *PT Ltd & Anor v Chief Executive, Department of Natural Resources and Water*.

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[1] *Kent Street Pty Ltd & Ors v Department of Natural Resources and Mines* [2008] QLAC 0221
[2] *Kent Street Pty Ltd & Ors v Department of Natural Resources and Mines* [2008] QLAC 0221
[3] See the Minister's media release dated 11 February 2010
[4] Section 3(1)(b) of the *Valuation of Land Act 1944*

In that decision, the Land Appeal Court determined that in calculating the unimproved value of improved land (in that case, the Chermside Shopping Centre), the valuer is to treat all improvements, including intangible improvements, as if they did not exist as at the date of the valuation. Significantly, the Land Court also noted that it was the role of the valuer to also consider the risks and costs associated with developing the notional vacant parcel of land. The Land Appeal Court held:

> *"...the valuation exercise required under Section 3(1)(b) for the subject land requires a valuer to proceed on the basis that, as at 1 October 2002, the improvements (including intangible improvements) did not exist and had never existed. However, the land is to be otherwise valued having regard to the environment in which it does exist. Relevantly for the subject land, that would include the services and amenities available to the land, any favourable and unfavourable statutory and/or local government rights or restrictions and, of particular importance in this case, the demographic features likely to influence the ability to attract an appropriate customer base and mix of tenants. Any potential the notionally vacant land has for a regional shopping centre should and must be taken into account, but that potential should not be treated as proved and effectively cost and risk free by reference to the past trading history of the site. In this context it is important to note that the reference to statutory and/or local government rights should not be seen as a reference to development approvals (DA's). "*

With respect to development approvals, the Land Appeal Court held that:

> *"...there is no reason why, as a matter of principle, a benefit conferred by a DA could not constitute an intangible improvement..."*

In early 2008, the State government, rather than pursing its appeal to the Court of Appeal against that decision, withdrew its appeal and instead introduced the *Valuation of Land Amendment Bill 2008* into Parliament. The Land Appeal Court recently said that the 2008 Bill "sought to "water down" if not defeat entirely, the force and effect of the decision"[5].

The retrospective 2008 Bill, as originally proposed, represented a significant departure from the valuation principles previously applied in assessing the unimproved value of land. Contrary to the State's assertions at the time, the 2008 Bill, as originally proposed, would have impacted on all types of property, including retail, commercial, industrial, tourist, residential and rural land, and would have effectively introduced a form of business tax by including the risk of obtaining the various approvals and bringing a property to its developed state (the development profit) in the unimproved value.

On 13 March 2008, in response to extensive lobbying from industry organisations, the State introduced amendments during the final debate on the 2008 Bill.

The amendments to the 2008 Bill removed the previous requirement in the 2008 Bill that the unimproved value of improved land was to include any increase in value connected with making or using an improvement on the land, and that in assessing the unimproved value, there was to be no risk in realising or continuing an existing use on the land.

Previously under the Act, the unimproved value of land was assessed on the basis that the land could be used for its present use but with the requisite approval for that use yet to be obtained. In other words, valuers were required to make an allowance for the time and cost involved in obtaining a development approval. Although the value of unimproved land is now to be assessed with any approvals in place, the Act was not amended to require that there is no risk in realising or continuing an existing use on the land.

While the amendments were a significant outcome for the property industry in Queensland at the time, the long-term effect of the 2008 Bill (as passed) remained unknown, and the State may have left it open to later argue that because certain intangible improvements (such as leases, licences and goodwill) are no longer specifically included within the definition of improvements, they are not to be treated as if they "did not exist" in assessing the unimproved value of improved land.

Those concerns came to fruition in an appeal to the Land Appeal Court concerning the unimproved valuation of land comprising the Pacific Fair Shopping Centre.

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[5] *Kent Street Pty Ltd & Ors v Department of Natural Resources and Mines* [2008] QLAC 0221

In the case of *Kent Street Pty Ltd & Ors v Department of Natural Resources and Mines* [2008], the State essentially argued that the amendments to the Act meant that the Land Appeal Court's decision in the earlier case of *PT Ltd & Anor v Chief Executive, Department of Natural Resources and Water* [2007] was not good law and that the unimproved value of improved land was now to include the added value that leases gave to the land, part of the goodwill associated with the business conducted on the land, and an amount for any development premium or profit and risk associated with its previous development.[6]

In this case, the State contended that the leases and trading history of Pacific Fair Shopping Centre must be taken into account in determining the unimproved value of the land. The Land Appeal Court summarised the valuation exercise contended for by the State in determining the unimproved value of improved land as follows:

> *"...the respondent says that the leases and trading history associated with the shopping centre must be brought into account. And, as a consequence, the unimproved value under s.3(1)(b) is, in effect, the improved value of the land (including among other things the added value the leases give to the land) less the value of improvements. The value of the improvements is essentially determined by reference to their replacement costs."*

In a significant outcome for the property industry in Queensland, the Land Appeal Court rejected the State's assertion. In doing so, the Court said that the position contended for by the State, if successful, would have amounted to a "radical change to the State's rating and land tax system"[7], affecting a variety of commercial properties "ranging from shopping centres of various sizes to central business district properties and various tourist attractions".[8]

On 16 January 2009, the State instituted an appeal in the Court of Appeal challenging the decision of the Land Appeal Court. On 22 December 2009, the Court of Appeal, in its decision in *Chief Executive, Department of Natural Resources and Mines v Kent Street Pty Ltd,* dismissed the State's appeal against the decision of the Land Appeal Court, which had rejected the State's assertion that the unimproved value of improved land (for the purposes of levying land tax and rates) included the added value of any leases, the goodwill associated with the business conducted on the land, and an amount for any development premium or profit and risk associated with its previous development.

The new Bill

On 11 February 2010, the State government elected to introduce the new Bill, rather than to seek leave to appeal the Court of Appeal's decision to the High Court. The amendments proposed in the new Bill are to be retrospective, applying to all valuations in effect from 30 June 2002, including those for which objections have already been lodged or for which appeals have been instituted.

Under the 2010 Bill, the State proposes that the unimproved value of land will now include, among other things, the development premium or profit and risk in the development process, any goodwill, the added value of leases and agreements for lease, and the value of any infrastructure charges that have paid. Further, in determining the value of any improvements on the land, the State proposes to only look at the lesser of the depreciated cost of construction of the improvements or any depreciated value as recorded in the owner's book of accounts.

A new process for making objections to valuations is proposed. While the State claims it is simply streamlining the objection process, the amendments proposed place an enormous burden on owners, and are likely to be unworkable given that an owner only has 45 days to prepare and lodge any objection. Under this new system, the following will apply:

- Owners will be required to pay a fee for lodging their objection (the amount is to be prescribed under a regulation).
- There will be an onus on an owner to provide a high level of detail with their objection (including, for example, in respect of improvements on the land, valuation reports, depreciation schedules and insurance assessments).

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[6] Although the appeal was instituted by the owners before the 2008 Bill was introduced and the amendments to the Act passed, the retrospective operation of the amendments meant that the Act as amended was the relevant legislation for the hearing of the appeal.
[7] *Kent Street Pty Ltd & Ors v Department of Natural Resources and Mines* [2008] QLAC 0221
[8] *Kent Street Pty Ltd & Ors v Department of Natural Resources and Mines* [2008] QLAC 0221

- If the State considers that the application is not properly made, an owner is given 14 days to amend the objection. If the State is still not satisfied, the objection is deemed to be not properly made. In that instance, the Land Court will no longer be able to make decisions as to whether an objection is properly made. An owner's only remedy in that situation would be to start judicial review proceedings in the Supreme Court.

- The State may require owners to provide further information that the State considers relevant. The failure to provide that information, if it exists, within 28 days will result in the objection lapsing.

- An owner's right of appeal to the Land Court for a decision on an objection is limited to the grounds contained in the objection.

The 2010 Bill also introduces a schedule of valuations that will document when valuation will be undertaken for each local government area for up to 10 years in advance, and a mechanism whereby a market adjustment factor will be used to adjust values in those years when a general valuation has not been undertaken for a particular area in that year. An owner will have no right of objection or appeal against a valuation that has increased as a consequence of the application of the market adjustment factor.

Implications

Investors and businesses need to be concerned about these amendments. The implications of the Bill are enormous. They include the following:

- There will undoubtedly be an increase in land valuations for commercial and industrial properties across the State.

- Land tax is paid at the rate of up to two cents in the dollar. In the case of companies, for example, for every $5 million increase in the unimproved land value, the amount of land tax payable per year will increase by $100,000. That will be borne by owners (including investors of superannuation funds) and will potentially impact tenants, either indirectly through market rent reviews, or directly in the case of non-retail tenants who have entered leases after 1 July 2009 that provide for the recovery of land tax.

- There will be a reduction in asset values as a consequence of the capitalisation of net income reduced though the increase in land tax and rates. This will have a significant impact on the value of investments held in superannuation funds.

- The reduction in asset values will make it more difficult to obtain finance, further impacting on the Queensland property sector.

- Increased charges will place pressure on small businesses and will lead to the loss of jobs.

- The changes are likely to act as a major disincentive to investment in Queensland.

Industry organisations have already expressed outrage at what has been described by the Property Council of Australia as "draconian legislation" and an "insult to the Queensland property industry"[9] Those industry organisations will undoubtedly make a concerted effort to lobby for changes to be made to the new Bill. If the behaviour of the State to date is anything to go by, however, changes would unfortunately appear unlikely.

For more information about the new Bill, or for help preparing an objection, please contact HopgoodGanim's Planning and Development practice.

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[9] Property Council of Australia media release dated 11 February 2010

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